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United States General Accounting Office
Washington, DC 20548

July 15, 2002

The Honorable John McCain
Ranking Minority Member
Committee on Commerce, Science, and Transportation
United States Senate

Subject: *Financial Management: Amtrak's Route Profitability Schedules Need Improvement*

Dear Senator McCain:

Each year, Amtrak must provide an Annual Operations Report to the Congress[1] that shows revenue, cost, and profit or loss on all its train routes in the form of route profitability schedules and an annual audited financial statement. The Congress uses the information provided on these schedules to help evaluate Amtrak's financial performance, including the profitability of individual Amtrak routes.

In addition, Amtrak periodically receives requests from the Congress or its staff to provide route profitability schedules at different times of the year. In response to such a request, in May 2001 Amtrak provided your staff with schedules that included comparative data for fiscal years 1999 and 2000. In November 2001, Amtrak provided schedules with data for fiscal year 2001 that also included data for fiscal years 1999 and 2000 that differed from the information previously provided in May. Also, it was not readily apparent how any of the schedules tied to Amtrak's audited financial statements. This letter summarizes the information provided during our briefing to your staff on May 14, 2002. The enclosed briefing slides highlight the results of our work and the information provided. You asked that we (1) determine the reasons for the differences between the totals on Amtrak's annual route profitability schedules for the same periods, and how the schedules correlate to the audited financial statements, and (2) comment on the general clarity and usefulness of the schedule presentations.

Results in Brief

In November 2001, Amtrak changed the way it prepared its route profitability schedules and applied this new method to information previously provided in May 2001 for fiscal years 1999 and 2000. Based on the initial information requested and provided, the schedule totals could not be readily reconciled to the audited financial statements for the corresponding periods. According to Amtrak officials, in order to focus on the operating

[1]Pursuant to Section 24315(a)(1) of Title 49, U.S. Code, Amtrak is required to provide this report, which includes revenue, cost, and profit or loss for all its train routes to the Congress no later than February 15th of each year.

profitability of its routes, Amtrak excluded certain items included in the financial statement amounts in preparing the route schedule data. As a result, the totals for both sets of schedules did not tie directly to the audited financial statements. In addition, for the November 2001 schedules, Amtrak changed the mix of these excluded items, which caused the differences between the two sets of schedules. The clarity and usefulness of the schedules provided to congressional staff were impaired because there was limited explanation of how these schedules were prepared, why they changed, and how they correlated to the audited financial statements. With Amtrak's assistance, we were able to reconcile both sets of schedules to the audited financial statements.

In the course of our work, we also noted that Amtrak allocated certain profits from its other business activities to its routes as a reduction in route net cost. According to Amtrak, it allocated these profits to partially offset the losses incurred on scheduled Amtrak routes. Prior to November 2001, Amtrak allocated these profits to all Amtrak routes in proportion to their share of total operating costs. In November 2001, Amtrak began allocating these profits only to routes with losses. Amtrak's allocation of these profits from its other business activities undermines the ability to assess whether or not individual routes are operated profitably. The more recent change to allocate those profits solely to routes operating at a loss further erodes the ability to compare the operating results of individual routes. Collectively, these practices compromise the usefulness of these schedules to help congressional decisionmakers assess route profitability.

Recommendations

To improve the clarity and usefulness of the route profitability schedules provided to congressional staff and others, we recommend that the President and Chief Executive Officer of Amtrak make the following changes.

- Provide a clear explanation of the methodology used in preparing the schedules, including how they correlate to the audited financial statements.
- Clearly explain any changes in the method for producing the profitability schedules on the face of the schedules.
- Discontinue the allocation of non-core profits to the route profitability schedules.

Agency Comments

We obtained oral comments on a draft of our briefing slides from Amtrak officials. Amtrak officials generally agreed with our findings and recommendations and their comments have been incorporated as appropriate. Amtrak officials made the following additional points: (1) Amtrak is asked to provide financial information on an expedited basis and in varying formats to a variety of organizations; (2) the schedules provided to the Congress in May and November 2001 were not part of Amtrak's reporting mandate to provide annual financial information on its train routes; and, (3) a detailed narrative explanation of changes made was provided in February 2002 in the mandated annual report. Amtrak officials agreed, however, that more clarity on the informal submissions would be appropriate.

Scope and Methodology

To fulfill our objectives, we reviewed the route profitability schedules provided in May 2001 and November 2001. Using the schedules, we (1) compared the fiscal years 1999 and 2000 total revenues, net cost, and profit or loss amounts presented in both sets of Amtrak schedules and discussed identified differences with Amtrak officials, (2) compared schedule totals to the audited financial statements, and (3) reviewed the schedule presentations for clarity and usefulness.

We did not review detailed data underlying the amounts reported in these schedules or assess Amtrak's route cost accounting methodologies. We conducted our work from February 20, 2002, through March 15, 2002, in accordance with generally accepted government auditing standards.

This report is available on our home page at *http://www.gao.gov*. If you have any questions about this report, please contact me at (202) 512-8341 or John C. Fretwell, Assistant Director, Financial Management and Assurance, at (202) 512-9382. You may also reach us by e-mail at *fretwellj@gao.gov* or *calboml@gao.gov*. Key contributors to this assignment were Lisa J. Crye, John C. Fretwell and Doris G. Yanger.

Sincerely yours,

Linda Calbom

Linda M. Calbom
Director, Financial Management and Assurance

Enclosure

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National Railroad Passenger Corporation (Amtrak)

Amtrak's Route Profitability Schedules Need Improvement

Briefing to Staff of the Committee on Commerce, Science, and Transportation, United States Senate

May 14, 2002

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Background

- Pursuant to Section 24315(a)(1) of Title 49, U.S. Code, Amtrak is required to provide an Annual Operations Report to Congress no later than February 15 of each year on revenue, cost, and profit or loss for all its train routes. Amtrak provides this information in the form of schedules called "Financial Performance of Scheduled Amtrak Routes." Congress uses this information to help evaluate the profitability of individual Amtrak routes.

- In addition to the required submission mentioned above, Amtrak periodically receives requests by Congress or its staff to provide these schedules at different times of the year. Schedules provided to congressional staff in May 2001 included comparative data for fiscal years 1999 and 2000. In November 2001, Amtrak provided schedules with data for fiscal years 1999 – 2001. The fiscal year 1999 and 2000 data provided in November 2001 was different than that provided in May 2001.

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Background (cont.)

- Section 24315(d) of Title 49, U.S. Code requires Amtrak to submit annual audited financial statements.

- It was not readily apparent how the schedule totals tied to the audited financial statements.

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Objectives

With regard to the schedules provided in May 2001 and November 2001, you requested that we

- determine the reasons for the differences between the annual schedule totals for the same periods, and how the schedules correlate to the audited financial statements, and
- comment on the general clarity and usefulness of the schedule presentations.

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Scope and Methodology

We reviewed the schedules provided in May 2001 and November 2001, and

- compared the fiscal years 1999 and 2000 total revenues, net cost, and profit or loss amounts presented in both sets of Amtrak schedules, and discussed identified differences with Amtrak officials,
- also compared schedule totals to the audited financial statements[1] and, with the assistance of Amtrak officials, reconciled schedule totals to the financial statements, and
- reviewed the schedule presentations for clarity and usefulness.

[1] At the time of our review, the fiscal year 2001 audited financial statements had not been issued.

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Scope and Methodology (cont.)

We did not review detailed data underlying the amounts reported in these schedules or assess Amtrak's route cost accounting methodologies.

We requested comments on a draft of these briefing slides from Amtrak. We received oral comments from Amtrak that were incorporated into these briefing slides as appropriate.

We conducted our work from February 20, 2002 through March 15, 2002 in accordance with generally accepted government auditing standards.

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Results in Brief

In November 2001, Amtrak changed the way it prepared its route profitability schedules and applied this new method to information previously provided for fiscal years 1999 and 2000.

The schedules provided to congressional staff included limited explanation of how these schedules were prepared, why they changed, and how they correlated to the audited financial statements.[2]

To focus on the operating profitability of its routes, Amtrak made certain adjustments to the financial statement amounts in preparing the route schedule data. In addition, because Amtrak allocated certain profits from its other business activities to the schedules, the clarity and usefulness of the schedules in helping Congressional decision makers assess route profitability was impaired.

[2] With Amtrak's assistance, we were able to reconcile the schedules to the audited financial statements.

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Results in Brief (cont.)

Clearly explaining the route profitability schedule preparation method and discontinuing the allocation of other business profits to the routes would improve the schedules.

We made several recommendations that will help clarify the schedule presentation and improve their usefulness.

Amtrak officials generally agreed with the substance of our briefing and recommendations, and provided oral technical and clarifying comments.

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Reasons for Differences

Amtrak changed the way it prepared the route profitability schedules in November 2001 and applied this new method to information previously provided for fiscal years 1999 and 2000. As shown in the following table, the route loss totals in the November 2001 schedules differed from the route loss totals in the schedules provided in May 2001.

	Route Loss (in millions)	
Fiscal Year	May 2001	November 2001
1999	$476.0	$511.3
2000	$471.2	$506.0

Based on the initial information requested and provided, these amounts could not be readily reconciled to the related audited financial statements for the corresponding periods.

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Reasons for Differences (cont.)

According to Amtrak officials, in order to focus on the operating profitability of Amtrak routes, Amtrak made certain adjustments to the financial statement amounts in preparing the route schedule data provided in May 2001 and November 2001, which is why the totals for both sets of schedules do not directly tie to the audited financial statements.

In addition, for the November 2001 schedules, they changed the mix of these excluded items, which caused the differences between the two sets of schedules.

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Reasons for Differences (cont.)

Prior to November 2001, Amtrak excluded the following revenues and expenses that were included in the financial statement amounts when preparing their route profitability schedules:

- Other Business (including Commuter) revenue and related expenses[3]
- Certain Corporate expenses (e.g., salaries & benefits, office rent)
- Federal and state capital payment revenues and related interest income on those payments[4]
- Depreciation expense
- The non-cash portion of employee post retirement insurance expense
- Cost of progressive overhauls[5]

[3] Other Business revenue and related expenses include items such as work for other railroads, and real estate operations and development. As discussed later, profit (termed non-core profit) from these other lines of business was added back to the route profitability schedules and resulted in reducing route net cost.

[4] Federal and state capital payments are grants to supplement passenger and other revenue generated from operations. These grants are to be used for modernizing the track and other infrastructure Amtrak owns, purchasing locomotives, passenger cars, and other rolling stock (such as mail cars and express cars).

[5] Progressive overhauls are phased equipment overhauls that are performed each year in lieu of a comprehensive, or "heavy" overhaul every 4 years.

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Reasons for Differences (cont.)

Amtrak officials advised us that they changed their schedule preparation method in November 2001 to better conform to a financial measurement concept that presents earnings before interest, taxes, depreciation, and amortization (EBITDA).[6] As a result, Amtrak no longer excludes:

- the non-cash portion of employee post retirement insurance expense
- the cost of progressive overhauls

Also, in keeping with the EBITDA measurement concept, Amtrak changed the way it accounted for interest expense. Under the old method, interest was included in the route schedule net cost. Under the new method, it is excluded.

[6] EBITDA is a financial measure used by many analysts and investors to assess a company's operating performance. It eliminates the items listed above which are typically included in the determination of net income.

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Reasons for Differences (cont.)

Amtrak stated that eliminating interest, taxes, depreciation and amortization, which removes the capital and financing expenses of the corporation, allows a clearer understanding of operating performance.

In order to provide comparability with fiscal year 2001 data, Amtrak applied the new method to restate schedule data for fiscal years 1999 and 2000.

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Clarity and Usefulness

Clarity and usefulness of the Amtrak route profitability schedules was impaired because

- the original schedule preparation methodology was not explained clearly,
- when the preparation method changed, it was not completely evident from the schedules what had changed and why, and
- based on the initial information requested and provided, annual totals presented in the schedules could not be readily reconciled to the related audited financial statements, which caused confusion for those analyzing Amtrak's financial results using both sources of information.

With Amtrak's assistance, we were able to reconcile the schedules to the audited financial statements.

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Clarity and Usefulness (cont.)

In the course of our work, we also noted that Amtrak allocated non-core profits to Amtrak routes as a reduction in route net cost.[7] According to Amtrak, non-core profits are allocated to partially offset the losses incurred on scheduled Amtrak routes.

Amtrak changed the allocation method in November 2001.

- Under the old method, non-core profits were allocated to all Amtrak routes in proportion to their share of total operating costs.
- Under the new method, Amtrak allocated non-core profits only to routes with losses.

The usefulness of the schedules under both methods is compromised by this allocation of non-core profits.

[7] Non-core profits include profits, if any, from other business activities such as work for other railroads, and real estate operations and development.

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Clarity and Usefulness (cont.)

The allocation of non-core profits to Amtrak routes undermines the ability to compare route profitability.

- Under both allocation methods, year-to-year comparisons of the profitability of a given route are distorted. Reported route profitability rises or falls with changes in non-core profits, which are unrelated to actual route performance.
- The new method that allocates non-core profits only to routes with losses further distorts comparisons of route profitability during a given year. Routes with losses appear to have lower losses, and the reported differences between profitable and unprofitable routes are diminished or possibly eliminated.

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Conclusions

- The route profitability schedules provided to congressional staff in May and November 2001 lacked transparency because there was little explanation of how the schedules were prepared, why they changed, and how they correlated to the audited financial statements.
- The allocation of non-core profits to routes undermines the ability to compare performance among scheduled routes.
- These preparation methods compromise the usefulness of the schedules to help Congressional decision makers assess route profitability.

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Recommendations

We recommend the President and Chief Executive Officer of Amtrak make the following changes to improve the clarity and usefulness of the route profitability schedules provided to congressional staff and others.

- Provide a clear explanation of the methodology used in preparing the schedules, including how they correlate to the audited financial statements.
- Clearly explain any changes in the method for producing the profitability schedules on the face of the schedules.
- Discontinue the allocation of non-core profits to the schedules.

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Agency Comments

Amtrak officials generally agreed with the substance of our briefing and recommendations, and provided oral technical and clarifying comments, which we incorporated as appropriate. They made the following additional points.

- Amtrak is asked to provide financial information on an expedited basis and in varying formats to a variety of organizations.
- The schedules submitted to Congress in May and November 2001 termed informal submissions by Amtrak officials, were not part of Amtrak's reporting mandate to provide annual financial information on its train routes.
- In February 2002, Amtrak did provide a detailed narrative explanation of changes made in the mandated annual report on the financial information on its train routes.

Amtrak officials agreed, however, that more clarity on the informal submissions is appropriate.

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